Internal Revenue Service

memorandum

CC:FS:TL-N-10494-91
CORP:LEGardner

date: DEC 17 1991

to: District Counsel, Houston CC:HOU
Attn: Sheri Wilcox

from: Assistant Chief Counsel (Field Service) CC:FS

subject: [redacted]

This is a written response to your request for Field Service Advice, dated September 19, 1991. Due to the urgency of your request, we initially sent you an informal field service advice memorandum. We are supplementing that advice with this formal field service advice memorandum as initially requested by your office.

ISSUE

Which corporation is the proper party to receive the statutory notices of deficiency for the years ended [redacted] of [redacted], [redacted], [redacted], [redacted], and [redacted].

CONCLUSION

In order to protect the position of the Service with respect to the taxable periods in question, we recommend that the district director take the various steps as described below.

FACTS

[redacted], (hereinafter [redacted]) was incorporated in Texas on [redacted]. [redacted] owned [redacted] percent of the outstanding stock of [redacted] from the date of incorporation until [redacted]. [redacted] was the parent of a consolidated group. [redacted] and its subsidiaries filed consolidated returns for fiscal year ended [redacted]. The last return filed by this group was for the fiscal year ended [redacted].

On [redacted], [redacted] formed [redacted] He owned [redacted] percent of the common stock of [redacted] The preferred stock of [redacted], was owned by family trusts. [redacted] formed [redacted], to function as a holding company and to act as the new common parent of the [redacted] consolidated group. It is not certain whether [redacted], became the holding company for the [redacted] group on [redacted], or at a later date. We will assume that [redacted], became the holding company by a drop-down

by [redacted] of his [redacted] stock to [redacted], on or shortly after [redacted].

On [redacted], [redacted], was incorporated in [redacted]. [redacted], was a wholly owned subsidiary of [redacted]. On [redacted], [redacted] was merged into DGC, Inc. On the same day, the name of [redacted], was changed to [redacted], (hereinafter [redacted]). [redacted], remained the sole shareholder of the surviving corporation, [redacted]. On [redacted], [redacted], a Nevada corporation, was authorized to do business in Texas. On [redacted], the name of [redacted] was changed to [redacted]. [redacted], remained the sole shareholder of [redacted]. [redacted], remains an active Nevada corporation as of the date of your request.

A corporate officer of [redacted], acting on behalf of [redacted], appointed [redacted], as attorney to represent [redacted] before the Internal Revenue Service on tax matters for the fiscal years ended [redacted], and [redacted] (Form 2848). This appointment was made after the merger. Therefore, the validity of this appointment is questionable. In [redacted], a corporate officer of [redacted], acting on behalf of [redacted], appointed [redacted] and [redacted], as attorneys to represent [redacted], before the Internal Revenue Service on tax matters for all the fiscal periods in question.

The group's tax return for the fiscal year ended [redacted], was received on [redacted]. The taxpayer applied for an automatic extension of time to file its income tax return which extended the period to file to [redacted] (Form 7004). The return lists [redacted] as the agent for the group and lists its EIN number as EIN # [redacted].

The group's tax return for the fiscal year ended [redacted], was received on [redacted]. The taxpayer applied for an automatic extension of time to file its income tax return which extended the period to file to [redacted]. The return lists [redacted] as the agent for the group and lists the same EIN number. The affiliation schedule (Form 851) for this taxable period lists [redacted] as the parent of the group and lists two subsidiary members in the group.

The group's tax return for the fiscal year ended [redacted], was filed in [redacted]. On [redacted], [redacted], on behalf of [redacted], signed an application for an automatic extension of time to file the group's income tax return, which extended the period for filing to [redacted]. On [redacted], [redacted], on behalf of [redacted], applied for an additional extension of time to file the group's income

tax return, which extended the period for filing to [redacted]. The return lists [redacted], as the agent for the group and lists its EIN number as EIN # [redacted]. The affiliation schedule for this taxable period lists [redacted], as the parent of the group and listed [redacted] subsidiaries. [redacted] of these subsidiaries include the [redacted] subsidiaries of the [redacted] group. [redacted] is also listed as a subsidiary of the [redacted], group.

With respect to the fiscal year ended [redacted], on [redacted], the Service received a Form 872, signed by [redacted], on behalf of [redacted], to extend the period of limitations to assess the group's income tax to [redacted]. Subsequently, on [redacted], the Service received a Form 872-A for [redacted] to extend this period until the taxpayer terminated its consent or the Service terminates the consent, or the Service mailed a notice of deficiency for such period. On [redacted], the Service received a Form 872-T, signed by [redacted], on behalf of [redacted], terminating the consent to extend the period of limitations on assessment of the group's income tax.

The group's tax return for the fiscal year ended [redacted], was received on [redacted]. A representative of [redacted], applied for an automatic extension of time to file the group's income tax return, which extended the period for filing to [redacted]. [redacted], on behalf of [redacted], applied for an additional extension of time to file the group's income tax return, which extended the period for filing to [redacted]. The return lists [redacted], as the agent for the group. The affiliation schedule for this taxable period, lists [redacted] as a subsidiary of the group.

On [redacted], the Service received a Form 872, signed by [redacted], on behalf of [redacted], to extend the period of limitations to assess the group's income tax for the fiscal year ended [redacted], to [redacted]. On [redacted], the Service received a Form 872-A, signed by [redacted], on behalf of [redacted], to extend the period of limitations for assessment of the group's income tax. Subsequently, on [redacted], the Service received a Form 872-T, signed by [redacted], on behalf of [redacted], terminating the special consent to extend the time to assess the group's income tax.

The group's return for the fiscal year ended [redacted], was received on [redacted]. [redacted], on behalf of [redacted], applied for an automatic

extension of time and an additional extension of time to file the group's income tax returns, which extended the period of filing to [redacted]. The return lists [redacted], as the agent for the group. The affiliation schedule lists [redacted] as a subsidiary of the [redacted], group.

On [redacted], the Service received a Form 872-A, signed by [redacted], on behalf of [redacted], to extend the period of limitations for assessment of the group's income tax. Subsequently, on [redacted], the Service received a Form 872-T, signed by [redacted], on behalf of [redacted], terminating the special consent to extend the time to assess the group's tax.

You have indicated that you were notified by the offices of the Secretary of State for the State of Texas and the State of Nevada that [redacted] did not survive the merger.

DISCUSSION

Assessment of the group's income tax for the taxable periods in question may be made on or before the ninetieth day after the Internal Revenue Service office considering the case receives a Form 872-T, Notice of Termination of Special Consent to Extend the Time to Assess Tax, from the taxpayer or under other circumstances not present here. The group's representative executed Form 872-T's for the fiscal years ended [redacted], [redacted], and [redacted]. The Internal Revenue Service office received these forms on [redacted]. The ninetieth day after [redacted], was [redacted]. Therefore, the Service had to issue notices of deficiencies for these taxable periods on or before [redacted]. You indicated that the period of limitations for issuing such notices would expire [redacted]. We note that we provided you with our conclusions on [redacted], prior to your estimation of the expiration of the period of limitations.

The group's return for the fiscal year ended [redacted], involves a purported job credit carryback from the fiscal year ended [redacted]. The group's return for the fiscal year ended [redacted], involves a purported NOL carryback from the fiscal year ended [redacted]. Form 872's to extend the period of limitations for assessment of the group's income tax were not required for the fiscal years ended [redacted] and [redacted] since these years remain open pursuant to sections 6501(h) and 6501(j).

The common parent of a consolidated group is the sole agent for each subsidiary in the group. Treas. Reg. § 1.1502-77(a). Thus, generally, the common parent is the proper party to receive the statutory notices of deficiencies for group members and is

the proper party to file a petition with the Tax Court. Treas. Reg. § 1.1502-77(a). Generally, the common parent for a particular consolidated return year remains the common parent agent for the group with respect to that year even though that corporation is no longer the common parent of that group when some action needs to be taken for that year.

There are exceptions to this general rule. First, the general rule does not apply when the common parent is not in existence at the time such action is necessary. The common parent is considered to have gone out of existence when it merges into another corporation and is not the surviving corporation.

In the instant case, there is uncertainty regarding whether or not [redacted] went out of existence on the date of the merger. The group's returns for years following the merger indicate that [redacted] may have survived the merger. At least, a [redacted], having the same EIN number as [redacted] is listed as a subsidiary of the group. However, you indicated that the offices of the Secretary of State for the State of Texas, the state of incorporation of [redacted], and the State of Nevada, have notified you that [redacted] was not the surviving corporation in the merger. Because of this uncertainty as to whether or not [redacted] remained in existence after the merger, we are providing advice to cover both possibilities.

Second, the general rule may not apply when the consolidated return group undergoes a reverse acquisition following the consolidated tax year in question.[1] A reverse acquisition, as defined in Treas. Reg. § 1.1502-75(d)(3), occurs when the common parent or any member of its consolidated return group (the acquiring corporation) acquires the stock or substantially all the assets of another corporation (the acquired corporation) and, after the acquisition, the shareholders of the acquired corporation as a result of owning stock of the acquired corporation (immediately before the acquisition) own (immediately after the acquisition) more than 50 percent of the fair market value of the outstanding stock of the acquiring corporation.

In the instant case, when [redacted], was formed, there is a possibility that the group underwent a reverse acquisition. In such a case, [redacted], acquired the stock of [redacted], the acquired corporation. The stockholder of [redacted], [redacted], as a result of owning stock of [redacted] (immediately before the acquisition), may have owned

---

[1] Although not relevant here, the general rule arguably also does not apply when there is a downstream transfer of the parent's assets or the parent undergoes an "F" reorganization, pursuant to Treas. Reg. § 1.1502-75(d)(2).

(immediately after the acquisition) more than [redacted] percent of the fair market value of the outstanding stock of [redacted] Therefore, it is conceivable that the consolidated group of [redacted] and subsidiaries underwent a reverse acquisition on [redacted]. It is also possible that the two transactions, the forming of the holding company and the merger could be treated as one reverse acquisition transaction. However, we do not have sufficient facts to reach such conclusions.

Furthermore, in the case of a reverse acquisition, the answer of which corporation is the proper party to issue a statutory notice of deficiency may also depend on whether the old common parent went out of existence prior to issuing the statutory notice. If [redacted] went out of existence prior to issuing the statutory notice, the rule in Southern Pacific would apply. In Southern Pacific Co. v. Commissioner, 84 T.C. 375 (1985), the old common parent went out of existence as part of a reverse acquisition. The Service's position in this case was that the new common parent would be the common parent agent not only for years subsequent to the reverse acquisition but also for years prior to the acquisition. If the rule in Southern Pacific applied, the new common parent, [redacted], would be the common parent agent of the continuing group for years prior to, as well as subsequent to, the reverse acquisition. Therefore, [redacted] would be the proper party to receive the statutory notice.

However, as long as [redacted] remains in existence, then the rule in Southern Pacific might not apply. This office has taken the position that the holding in Southern Pacific only applies where the old common parent goes out of existence in a reverse acquisition. Where the old common parent remains in existence after the reverse acquisition, the position of this office is that the old common parent remains the proper party to receive the statutory notice, pursuant to Treas. Reg. § 1.1502-77(a). Hence, in applying this position to the instant case, [redacted] would be the proper party to receive the statutory notice.

Yet, the above-described limitation on the holding of Southern Pacific has not been tested in any court. In addition, the primary rule of Southern Pacific has not been tested in any appellate forum. Due to the uncertainty in this area, this office has adopted a precautionary approach to determining the proper party to execute consents and to receive deficiency notices. In such cases, the Service chooses to deal directly with the individual members of the consolidated group. Pursuant to Treas. Reg. § 1.1502-77(d), when the common parent goes out of existence and does not designate another member to act as agent for the group and the remaining members of the group do not designate such an agent, then the district director may choose to

deal directly with any member in respect to its liability. If the parent remains in existence and the Service wishes to deal directly with the members of the group, it must first notify the common parent that it has chosen to deal directly with these members. Therefore, when there is a question as to whether the common parent is still in existence at the time an action needs to be taken, it is usually advisable to deal with each member of the group separately, but only after sending notification to any possible common parent of such intention. See Treas. Reg. § 1.1502-77(d) and the last sentence of Treas. Reg. § 1.1502-77(a).[2]

Because there are three variables in this case that we are unable to determine, we have made our recommendations to protect the Service under various scenarios. The three variables are:

1. Whether there was a reverse acquisition;

2. Whether [redacted] survived the merger; and

3. When the group undergoes a reverse acquisition and the old common parent survives, which corporation, under current law, i.e., construing the rule of Southern Pacific, would be treated as the common parent.

We have listed below the steps that we recommend be taken by the district director with respect to each year.

FISCAL YEARS ENDED [redacted], [redacted], AND [redacted]

[redacted], was the common parent agent for the group during the taxable periods in question. According to the facts, [redacted], is currently an active corporation. Therefore, [redacted], is the proper party to receive the statutory notice of deficiencies for these taxable periods. The notices of deficiencies should be sent to [redacted], as agent for the affiliated group, [redacted]. These deficiency notices should indicate that they pertain to the consolidated tax liability of [redacted].

FISCAL YEARS ENDED [redacted] AND [redacted]

During these taxable periods, [redacted] was the common parent agent of the group. Due to the uncertainty of whether

---

[2] Pursuant to Treas. Reg. § 1.1502-6(a), the common parent and each subsidiary in the group are each severally liable for the total tax liability of the consolidated group.

[redacted] survived the merger and whether the group in question underwent a reverse acquisition, the Service must take a protective position. Pursuant to Treas. Reg. § 1.1502-6(a), the common parent and each subsidiary which was a member of the group during any part of the consolidated return year is severally liable for the tax for such year. Pursuant to Treas. Reg. § 1.1502-77(d), if the district director has reason to believe that the common parent went out of existence, the district director may deal directly with any member of the group with respect to its liability. Alternative separate notices should be sent to the parties, as listed below:

1. [redacted], as agent of the affiliated group, [redacted]. This notice should indicate that it pertains to the consolidated tax liability of [redacted]. This protects the Service in the event the [redacted] group underwent a reverse acquisition and we assume that the rule of Southern Pacific applies, regardless of whether or not [redacted] continued in existence, so that [redacted], became the agent of that group for these tax years.

2. [redacted], formerly [redacted], as agent of the affiliated group, [redacted]. This notice should indicate that it pertains to the consolidated tax liability of [redacted]. This will protect the Service in the event of either of two possible scenarios. In both scenarios, we assume that [redacted] survives the merger. Under the first, the group did not undergo a reverse acquisition. Under the second scenario, the group underwent a reverse acquisition, but the rule in Southern Pacific is not applicable.

3. Assuming that [redacted], went out of existence per its merger with [redacted], and that the group did not undergo a reverse acquisition so that the rule of Southern Pacific does not apply, the following additional deficiency notices are required to protect the Service:

(a) Separate deficiency notices should be sent to each subsidiary. These notices should include the total tax liability since each subsidiary is severally liable for the tax liability of the consolidated group. Each notice should state the name of the subsidiary, with a note added by asterisk that "this is with respect to your separate, several liability for the consolidated tax of the affiliated group, [redacted].

(b) A deficiency notice should be sent to [redacted] This notice of deficiency should be headed "[redacted], (formerly [redacted], formerly [redacted]), as successor of

[redacted]." This notice should also include a note by asterisk that "this notice pertains to the consolidated tax liability of [redacted]. The proper EIN would be the EIN of [redacted].

4. Finally, it would be appropriate to issue a Notice of Transferee Liability with respect to the tax liability of [redacted] Inc. The notice should be headed [redacted], (formerly [redacted], formerly [redacted]), as transferee of [redacted].

This document may include confidential information subject to the attorney-client and deliberate process privileges, and may also have been prepared in anticipation of litigation. This document should not be disclosed to anyone outside the IRS, including the taxpayer involved, and its use within the IRS should be limited to those with a need to review the document in relation to the subject matter or case discussed herein. This document also is tax information of the instant taxpayer which is subject to I.R.C. § 6103.

If you have any questions regarding this matter, please contact Lorraine E. Gardner at (FTS) 566-3335.

DANIEL J. WILES

By: Steven J. Hankin
STEVEN J. HANKIN
Special Counsel (Corporate)
Field Service Division